Quadrant
A Quarterly Update
WINDHAVEN
INVESTMENT MANAGEMENT

Full Speed Ahead!

January 2018

Key Points:

1 2017 recap: The global economy displayed strong fundamentals; global equity markets experienced double-digit returns

2 2018 outlook: Acceleration of U.S. and global growth; the surprise of 2018 might be the return of inflation

3 Current positioning: Equities strongly favored

Looking Back at 2017

The past year was quite remarkable in many respects. The global economy displayed strong fundamentals; global equity markets experienced double-digit returns with unusually low volatility amid political and geopolitical uncertainty; the U.S. Congress overhauled the tax system; the U.S. Federal Reserve (Fed) increased interest rates three times in a year for the first time in over a decade; and Italy did not qualify for the 2018 Soccer World Cup for the first time in 60 years.

Italy did much better in the markets than in soccer with U.S. dollar based equity returns of nearly 30%.[1] Even better was the performance of emerging market equities such as India, China, and South Korea. This is emblematic of a year in which international equities benefited from an upswing in global economic fundamentals, favorable valuations, strong earnings growth, positive behavioral qualities, such as momentum, and a weaker U.S. dollar.

Looking Ahead

Our investment process evaluates where opportunities exist in a disciplined, quantitative way. We start by analyzing the state of the global economy, identifying asset classes which we believe are likely to generate attractive risk-adjusted returns. In addition to strong economic and fundamental drivers, we also look for asset classes with behavioral support. When we analyze the U.S. economy now, we see a ninth straight year of expansion for the U.S. economy and few signs that a recession or bear market is imminent. The recent U.S. tax reform may already be fully discounted into U.S. equity prices, but we believe it is likely to contribute to U.S. economic growth in 2018 and lengthen this expansion. Stronger growth in the United States and continued growth outside the United States should be supportive of global equities which remain reasonably priced, are backed by strong economies, and exhibit attractive behavioral characteristics.

With an acceleration of U.S. and global growth, the surprise of 2018 might be the comeback of inflation – at least enough to keep the Fed on track with interest rate hikes and balance sheet contraction, and enough to get the European Central Bank to start making and communicating a plan of its own for policy normalization. With these policy dynamics, the course of the U.S. dollar is likely, again, to have a significant impact on equity returns. That said, we believe, the tightening of monetary policy in a growing global economy will likely mean that equities continue to outperform bonds.

Geopolitical risk has been largely dwarfed by positive fundamentals over the past year. As we move deeper into expansion, it is possible geopolitical risk or a disappointment in growth relative to expectations might cause more volatility in equity prices. We continue to stay true to our process, striving to continue capturing market upside, while carefully managing risk and remaining diversified.

Fig 1: Currency market gyrations | *Source: Bloomberg as of 12/31/2017.*

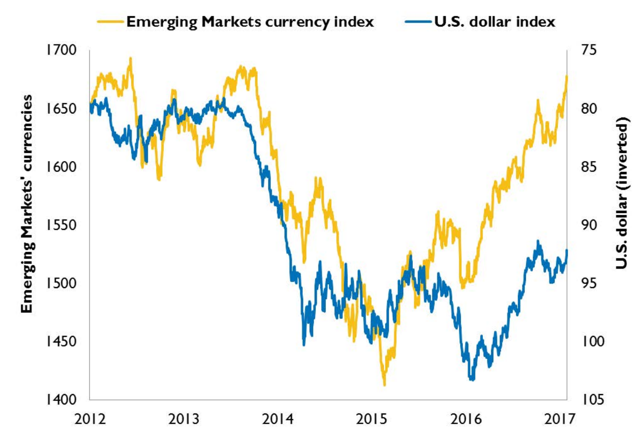
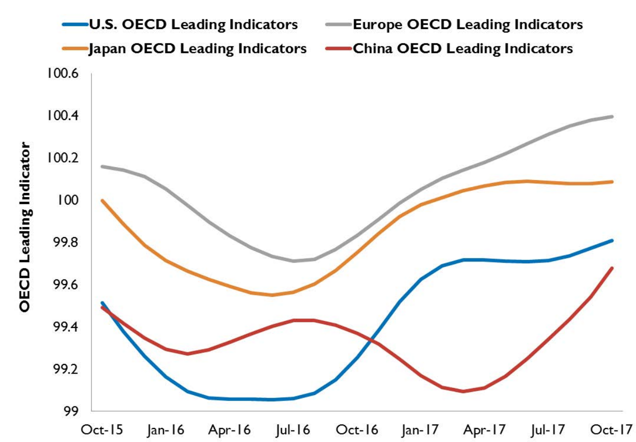


Fig 2: Organisation for Economic Co-operation & Development (OECD) leading indicators | *Source: Organisation for Economic Co-operation and Development & Bloomberg as of 10/31/2017.*



Positioning

As was the case for the first nine months of 2017, the Windhaven Diversified Strategies strongly favored equities in the fourth quarter as behavioral characteristics remained strong, valuations were reasonable, and the growing economy supported equities. Adjustments to the strategies during the quarter resulted in a net increase to our equities holdings, with a growing preference for international equities based on higher growth rates and more favorable valuations in many areas. At year-end, nearly two-thirds of the equity holdings in our Diversified Growth and Diversified Aggressive strategies consisted of developed international and emerging markets equities, while in our Diversified Conservative strategy, they accounted for a bit more than half. While the allocation to equities rose, it did so mostly at the expense of U.S. and international fixed income securities. We remain cautious on fixed income securities, with below-average exposures in each strategy while also carefully managing our duration or the sensitivity to changes in interest rates. The low level of interest rates we see in the

United States and outside are inconsistent with our economic readings which suggest economic strength. Our allocation to hard assets is on the lower end of our historical allocations as we simply see more attractive opportunities in equities. However, as we enter 2018 the conditions in the commodity markets appear more attractive than they have been for several years and we are alert to the potential that commodities could be becoming better investments. While our outlook continues to be bullish for the economy and equities if the environment changes our positioning will change as well.

We appreciate your investment in Windhaven and look forward to 2018. Please contact your Investment Professional if your investment objectives or circumstances have changed such that a review of your Windhaven strategy might be necessary, or if you have any specific questions about how your account is managed. We value the trust our clients have placed in us, and we are passionate about the Windhaven strategies and the role they play in helping each of you reach your investment goals.

-Portfolio Management Team

Fig 3: Earnings growth across regions | *Source: Bloomberg as of 12/31/2017 | Trailing 12-month EPS for MSCI ACWI (global), MSCI USA, MSCI Emerging Markets, MSCI EAFE (developed markets ex U.S.). Growth in EPS based to 1/31/2016 = 100%.*

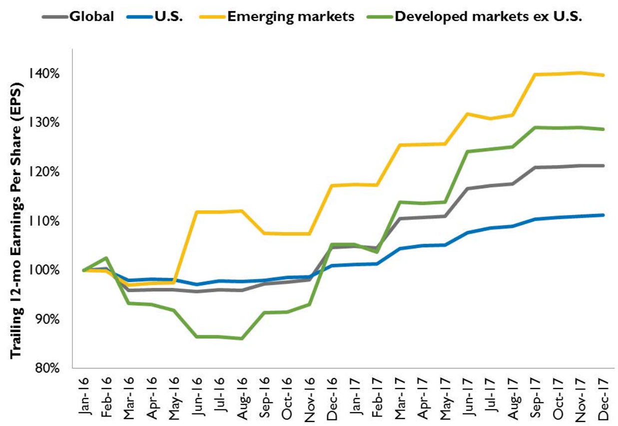
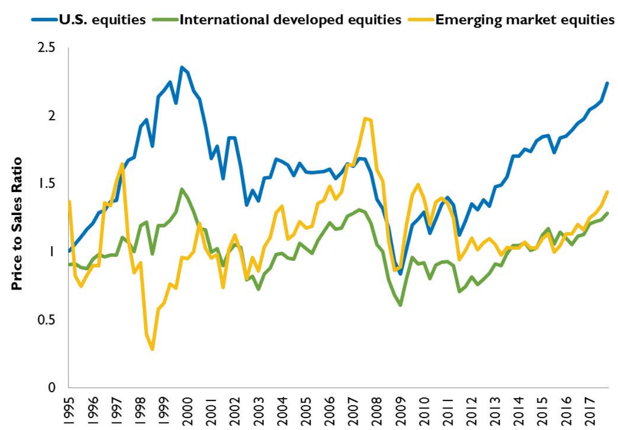


Fig 4: Global equity valuations | *Source: Bloomberg as of 12/31/2017. U.S. equities are represented by MSCI USA, Emerging market equities are represented by MSCI Emerging Markets, International developed equities are represented by MSCI EAFE.*



[1]Source: Bloomberg 1/1/2017-12/31/2017

Important Notes and Disclosures:

The information provided herein is for general informational purposes only and should not be considered an individualized recommendation or personalized investment advice. The investment strategies mentioned here may not be suitable for everyone. Each investor needs to review an investment strategy for his or her own particular situation before making any investment decision.

All expressions of opinion are subject to change without notice in reaction to shifting market conditions. Data contained herein from third party providers is obtained from what are considered reliable sources. However, its accuracy, completeness or reliability cannot be guaranteed.

Indexes shown in the charts throughout are unmanaged, do not incur fees or expenses, and cannot be invested in directly.

Past performance is no guarantee of future results.

International investments may involve additional risks, which could include differences in financial accounting standards, currency fluctuations, political instability, foreign taxes and regulations, and the potential for illiquid markets. Investing in emerging markets may accentuate these risks.

Fixed income securities are subject to increased loss of principal during periods of rising interest rates. Fixed income investments are subject to various other risks including changes in credit quality, market valuations, liquidity, prepayments, early redemption, corporate events, tax ramifications and other factors.

Hard assets can be significantly affected by commodity prices, world events, import controls, worldwide competition, government regulations, and economic conditions.

Windhaven's risk management process includes an effort to monitor and manage risk, but should not be confused with and does not imply low risk or the ability to control risk.

Portfolio management for the Windhaven Strategies is provided by Windhaven Investment Management, Inc. ("Windhaven"), a registered investment adviser. Windhaven and Charles Schwab & Co., Inc. are separate but affiliated companies and subsidiaries of The Charles Schwab Corporation.

Please refer to Windhaven's ADV Part 2 for additional information.

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